APPENDIX

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 14. SURTAX ON UNDISTRIBUTED PROFITS.

(a) *Definitions.*—As used in this title—

(1) The term "adjusted net income" means the net income minus the sum of—

(A) The normal tax imposed by section 13.

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(2) The term "undistributed net income" means the adjusted net income minus the sum of the dividends paid credit provided in section 27 and the credit provided in section 26 (c), relating to contracts restricting dividends.

(b) *Imposition of tax.*—There shall be levied, collected, and paid for each taxable year upon the net income of every corporation a surtax equal to the sum of the following, subject to the application of the specific credit as provided in subsection (c):

[Here follow graduated rates.]

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SEC. 26. CREDITS OF CORPORATIONS.

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

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(c) *Contracts restricting payment of dividends.*—

(1) *Prohibition on payment of dividends.*—An amount equal to the excess of

the adjusted net income over the aggregate of the amounts which can be distributed within the taxable year as dividends without violating a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the payment of dividends. If a corporation would be entitled to a credit under this paragraph because of a contract provision and also to one or more credits because of other contract provisions, only the largest of such credits shall be allowed, and for such purpose if two or more credits are equal in amount only one shall be taken into account.

(2) *Disposition of profits of taxable year.*—An amount equal to the portion of the earnings and profits of the taxable year which is required (by a provision of a written contract executed by the corporation prior to May 1, 1936, which provision expressly deals with the disposition of earnings and profits of the taxable year) to be paid within the taxable year in discharge of a debt, or to be irrevocably set aside within the taxable year for the discharge of a debt; to the extent that such amount has been so paid or set aside. For the purposes of this paragraph, a requirement to pay or set aside an amount equal to a percentage of earnings and profits shall be considered a requirement to pay or set aside such percentage of earnings and profits. As used in this paragraph, the word "debt" does not include a debt incurred after April 30, 1936.

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Revenue Act of 1942, Public Law 753, 77th Congress, 2d Session:

SEC. 501. ADDITIONAL CREDITS FOR UNDISTRIBUTED PROFITS TAX.

(a) *Amendments to the Revenue Act of 1936.*—

(1) Section 14 (a) (2) of the Revenue Act of 1936 (relating to definition of undistributed net income) is amended to read as follows:

"(2) The term 'undistributed net income' means the adjusted net income minus the sum of (A) the dividend paid credit provided in section 27, (B) the credit provided in section 26 (c) relating to restrictions on payment of dividends, (C) except in cases where section 26 (c) (1) is applicable, the deficit credit provided in section 26 (f), and (D) the redemption credit provided in section 26 (g)."

(2) Section 26 (c) of the Revenue Act of 1936 (relating to credits of corporations) is amended by amending the heading to read as follows: "(c) *Restrictions on payment of dividends.*—"; and by amending paragraph (3) to read as follows:

"(3) *Deficit corporations.*—In the case of a corporation having a deficit in accumulated earnings and profits as of the close of the preceding taxable year, the amount of such deficit, if the corporation is prohibited by a provision of a law or of an order of a public regulatory body from paying dividends during the existence of a deficit in accumulated earnings and profits, and if such provision was in effect prior to May 1, 1936.

"(4) *Double credit not allowed.*—If more than one of the credits provided in the foregoing paragraphs (1), (2), and (3) apply, then the paragraph which allows the greatest credit shall be applied; and, if the

credit allowable under each paragraph is the same, only one of such paragraphs shall be applied."

(3) Section 26 of the Revenue Act of 1936 (relating to credits of corporations) is amended by adding at the end thereof the following new subsections:

"(f) *Deficit credit.*—The amount by which the adjusted net income exceeds the sum of (1) the earnings and profits accumulated after February 28, 1913, as of the beginning of the taxable year, and (2) the earnings and profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year). For the purposes of this subsection, earnings and profits of the taxable year shall be computed without diminution by the amount of the tax imposed under section 14, 102, 103, or 351 for such taxable year; and earnings and profits accumulated after February 28, 1913, as of the beginning of the taxable year, shall be diminished on account of the tax under section 14, 102, 103, or 351 for any previous taxable year only by the amount of such tax as computed under the amendments made by section 501 of the Revenue Act of 1942.

* * * * *

(b) *Effective date of amendments.*—The amendments made by subsection (a) shall be effective as of the date of the enactment of the Revenue Act of 1936.

(c) *Overpayments.*—If the refund or credit of any overpayment for any taxable year, to the extent resulting from the application of this section, is prevented on the date of the enactment of this Act or within one year from such date, then, notwith-

standing any other provision of law or rule of law (other than this subsection and other than section 3761 of the Internal Revenue Code or section 3229 of the Revised Statutes, or such section as amended by section 815 of the Revenue Act of 1938, relating to compromises), such overpayment shall be refunded or credited in the same manner as in the case of an income tax erroneously collected under the Revenue Act of 1936, if claim therefor is filed within one year from the date of the enactment of this Act.

Treasury Regulations 94, promulgated under the Revenue Act of 1936:

ART. 26–2. *Credit in connection with contracts restricting payment of dividends.*— (a) The credit provided in section 26 (c) with respect to contracts restricting the payment of dividends is not available under every contract which might operate to restrict the payment of dividends, but only with respect to those provisions of written contracts executed by the corporation prior to May 1, 1936, which satisfy the conditions prescribed in the Act. The charter of a corporation does not constitute a written contract executed by the corporation within the meaning of section 26 (c). The provisions recognized by the Act are of two general types, as follows:

(1) Those which come within section 26 (c) (1), in that they prohibit or limit the payment of dividends during the taxable year; and

(2) Those which come within section 26 (c) (2), in that they require the payment, or irrevocable setting aside, within the taxable year, of a specified portion of the

earnings or profits of the taxable year for the discharge of a debt incurred on or before April 30, 1936.

If a corporation is restricted with respect to the payment of dividends by two or more contract provisions coming within section 26 (c) (1), only the largest of the credits computed with respect to each of such provisions, and not their sum, shall be allowable under section 26 (c) (1) and, for such purpose, if two or more credits are equal in amount, only one shall be taken into account. However, section 26 (c) (3) provides that if both section 26 (c) (1) and section 26 (c) (2) apply, only the one of such paragraphs which allows the greater credit shall be applied, and, if the credit allowable under each paragraph is the same, only one of such paragraphs shall be applied.

(b) *Prohibition on payment of dividends.*—The credit provided in section 26 (c) (1) is allowable only with respect to a written contract executed by the corporation prior to May 1, 1936, which expressly deals with the payment of dividends and operates as a legal restriction upon the corporation as to the amounts which it can distribute within the taxable year as dividends. If an amount can be distributed within the taxable year as a dividend—

(1) in one form (as, for example, in stock or bonds of the corporation) without violating the provisions of a contract, but cannot be distributed within the taxable year as a dividend in another form (as, for example, in cash) without violating such provisions, or

(2) at one time (as, for example, during the last half of the taxable year) without

violating the provisions of a contract, but cannot be distributed as a dividend at another time within the taxable year (as, for example, during the first half of the taxable year) without violating such provision—

then the amount is one which, under section 26 (c) (1), can be distributed within the taxable year as a dividend without violating such provisions.

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U. S. GOVERNMENT PRINTING OFFICE: 1942